

Financial Forecast

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Financial Forecast

The following forecast provides preliminary projections for FY 2007 and FY 2008 by maintaining the FY 2006 Adopted Budget Plan Real Estate Tax rate of \$1.00 and limiting increases in County expenditures and the transfer to the Schools to the revenue growth rate anticipated in each year. This forecast projects County total revenue growth of 7.61 percent in FY 2007 and 6.91 percent in FY 2008. These rates of growth are due to projected moderating increases in real estate property values and decelerating growth in other revenue categories. Sales Tax receipts, for example, experienced robust growth of 10.5 percent in 2004. The Budget estimate for this category shows moderation in FY 2005 and FY 2006 which is expected to continue into the forecast period. Excluding Real Estate Tax revenue, all other categories are anticipated to increase just 3.7 percent and 3.4 percent in FY 2007 and FY 2008, respectively. This current forecast shows deficits of \$31.3 million in FY 2007 and \$29.3 million in FY 2008.

During their deliberations on the FY 2006 Adopted Budget Plan, the Board of Supervisors adopted a series of budget guidelines which will limit County and school spending. For the FY 2007 budget, staff will be developing a forecast that incorporates the Board's Budget Guidelines. The revised forecast will incorporate more detailed information on projected revenue growth for all revenue sources and anticipated cost required of both the County and Schools for the forecast period.

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FY 2007 and FY 2008 FINANCIAL FORECAST (millions)

	FY 2004 ACTUAL	FY 2005 REVISED	FY 2006 ADOPTED	FY 2007 FORECAST	FY 2008 FORECAST
Available Beginning Balance	\$118.89	\$99.26	\$35.52	\$0.00	\$0.00
Reserves Balance	0.00	53.08	57.17	60.42	64.85
REVENUE:					
Real Estate Taxes	\$1,500.73	\$1,634.41	\$1,776.08	\$1,958.31	\$2,137.84
Personal Property Taxes ¹	473.87	468.04	481.99	500.94	518.19
Other Local Taxes	408.23	449.80	461.10	474.80	489.10
Permits, Fees, and Licenses	28.68	27.58	32.54	34.09	34.24
Fines and Forfeitures	13.27	12.89	12.28	12.52	12.77
Revenue from Use of Money/Property	17.92	29.20	41.62	49.63	58.98
Charges for Services	42.53	44.73	49.46	52.14	53.35
Revenue from the Commonwealth ¹	83.56	80.71	81.41	81.41	81.41
Revenue from the Federal Govt.	56.63	43.18	43.19	43.19	43.19
Recovered Costs/Other Revenue	6.49	6.59	6.59	6.59	6.59
TOTAL REVENUE	\$2,631.92	\$2,797.12	\$2,986.26	\$3,213.62	\$3,435.66
TRANSFERS IN	1.40	1.67	2.60	2.10	2.16
TOTAL RECEIPTS	\$2,633.31	\$2,798.79	\$2,988.86	\$3,215.72	\$3,437.82
TOTAL AVAILABLE	\$2,752.21	\$2,951.13	\$3,081.55	\$3,276.15	\$3,502.67
DIRECT EXPENDITURES:					
Personnel Services	\$525.89	\$567.37	\$624.27	\$671.80	\$718.22
Operating Expenses	308.17	360.57	321.41	345.88	369.78
Worked Performed for Others	(36.78)	(42.25)	(40.89)	(44.01)	(47.05)
Capital Equipment	3.37	6.57	2.71	2.92	3.12
Fringe Benefits	132.81	161.72	176.48	189.91	203.03
TOTAL DIRECT EXPENDITURES	\$933.47	\$1,053.98	\$1,083.97	\$1,166.50	\$1,247.09
TRANSFERS OUT:					
Schools	\$1,240.85	\$1,322.37	\$1,431.34	\$1,540.31	\$1,646.74
G O Debt (County)	98.45	98.72	98.72	112.56	117.94
G O Debt (Schools)	120.90	126.53	130.28	148.60	155.70
CSB	80.60	82.07	90.98	97.90	104.67
Metro	12.27	18.14	21.32	24.51	28.19
Paydown Construction	41.17	60.58	29.09	10.00	10.00
County Transit	19.65	21.36	24.15	25.98	27.78
Other Transfers	35.93	51.66	62.10	66.82	71.44
Stormwater Management Program	0.00	0.00	17.90	19.70	21.60
Housing Flexibility Fund	0.00	0.00	17.90	19.70	21.60
Information Technology	11.33	11.42	13.41	10.00	10.00
Revenue Stabilization	5.25	11.62	0.00	0.00	0.00
TOTAL TRANSFERS OUT	\$1,666.39	\$1,804.46	\$1,937.16	\$2,076.10	\$2,215.66
TOTAL DISBURSEMENTS	\$2,599.86	\$2,858.44	\$3,021.13	\$3,242.60	\$3,462.75
ENDING BALANCE	\$152.34	\$92.69	\$60.42	\$33.55	\$39.92
Managed Reserve	53.08	57.17	60.42	64.85	69.25
TOTAL AVAILABLE	\$99.26	\$0.00	\$0.00	(\$31.31)	(\$29.33)

¹The portion of the Personal Property Tax reimbursed by the Commonwealth as a result of the Personal Property Tax Relief Act of 1998 is included in the Personal Property Tax category for the purpose of discussion in this section.

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Revenue Assumptions

Revenue estimates for FY 2007 and FY 2008 are based on a review of current and projected local and national economic conditions. Most economists expect that national economic growth will slow somewhat from the robust pace of 2004. Real economic growth, as measured by the Gross Domestic Product (GDP), increased 4.4 percent in 2004. In the first quarter of 2005; however, economic growth slowed to a rate of 3.1 percent. The Consumer Confidence Index, an indicator of future consumer spending, rose in May after falling in April. The U.S. Leading Index of Economic Indicators decreased in April 2005 for the fourth consecutive month. The recent weakness of the Leading Index is consistent with the economy continuing to expand in the near term, but at a somewhat slower pace.

Growth in the Fairfax County economy was exceptionally strong in 2004. Gross County Product, an estimate of the goods and services produced in the County, rose a revised 6.2 percent, the fastest pace since 2000. An estimated 25,000 net new jobs were created in Fairfax County in 2004, an increase of 4.1 percent over 2003. This increase is primarily due to increased federal procurement spending. Favorable interest rates have also advanced the economy by spurring consumer spending, home purchases and business investment.

Fairfax County's real economic growth is expected to moderate throughout the forecast period. Economic forces that fueled robust growth in 2004, such as rapid federal spending, low interest rates and federal tax cuts are expected to dissipate, resulting in more measured growth. Based on Dr. Fuller's May 2005 projections, economic growth in Fairfax County is expect to slow from the 6.2 percent increase experienced in 2004 to 5.2 percent and 4.2 percent in FY 2005 and FY 2006, respectively. During the forecast period, economic growth is expected to moderate further to 4.1 percent in FY 2007 and 3.9 percent in FY 2008.

Fairfax County's Leading Index, which is designed to forecast the performance of the County's economy nine to twelve months in advance, increased in March 2005 for the fourth consecutive month. However, gains in the Index have slowed which indicates that the economy is transitioning from acceleration to a pattern of more stable growth. The moderating of the County's economy, according to Dr. Stephen Fuller is primarily due to an increase in energy costs.

FY 2006 represents the fifth year of double-digit increases in Fairfax County residential assessments. Since FY 2001, the mean assessed value of a home in Fairfax County has risen approximately 114 percent. During this period, spending by the federal government was increased significantly as a result of post-September 11, 2001 homeland security spending. Job growth created a demand for housing that exceeded the supply of available homes. These factors, along with historically low interest rates have propelled home prices upward.

While there is no expectation of price declines, the rapid rise in housing values over the past several years has raised concerns of a potential housing "bubble." The rise in home prices has been much faster than the rise in incomes. By comparing home prices to incomes, the Local Market Monitor estimated that homes in the Washington Area are overvalued by 17 percent. As housing prices have consistently risen for a number of years, analysts believe speculative purchases have increased. Buyers may be willing to offer more for a home when there is the expectation of continued appreciation. This view is echoed by information presented at a National Association of Home Builders' (NAHB) conference in October 2004. The NAHB indicated that the Washington area is one of 14 metropolitan areas they consider to be overpriced. The current level of price appreciation is not expected to continue into FY 2007 and FY 2008. A gradual rise in mortgage interest rates and slower economic growth are expected to cool the housing market during the forecast period. Sixteen economists and executives that follow the Washington Metropolitan Area were surveyed in January 2005 by *The Washington Post*; their median projection for 2005 single-family home appreciation in the region was 8.9 percent (2005 home values will be reflected in FY 2007 assessments).

The Financial Forecast assumes an overall increase in Real Estate values of 10.30 percent in FY 2007 and 9.20 percent in FY 2008 compared to the 23.49 percent increase experienced in FY 2006. Total equalization, or the reassessment of existing property, is anticipated to increase 8.20 percent in FY 2007 and 7.40 percent in FY 2008. Residential equalization is projected to increase at moderate rates of 9.00 percent in FY 2007 and 8.00 percent in FY 2008.

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In FY 2006, existing nonresidential property values experienced a robust increase of 12.74 percent after rising just 3.74 percent in FY 2005 and declining 2.94 percent in FY 2004. As a result of improving office vacancy rates and recent sales activity, the value of Office Elevator properties (mid- and high-rises), which comprise 37.2 percent of the nonresidential tax base, rose 18.81 percent in FY 2006. The Economic Development Authority (EDA) recently reported that the office vacancy fell below double digits to 9.7 percent at mid-year 2004 from 11.2 percent as of year-end 2003. Including sublet space, the office vacancy rate fell from 15.6 percent as of year-end 2003 to 13.3 percent as of mid-year 2004. Office vacancy rates are expected to continue to improve during the forecast period as a result of business expansion and job growth.

The value of Hotel property advanced a hearty 15.34 percent in FY 2006 after increasing 4.48 percent in FY 2005. Lower rates of growth are projected in Hotel property over the next two years as occupancy rates drop slightly in response to the additional availability of rooms as two new hotels were delivered in late 2004 and two are expected to be completed in 2005, increasing room inventory 4.0 percent. The Retail and Regional Malls categories rose 10.99 and 4.06 percent, respectively in FY 2006. Growth in these categories is expected to be lower during FY 2007 and FY 2008 in response to slower growth in the economy. Overall, the value of existing nonresidential properties is anticipated to experience moderate increases of 5.00 percent in both FY 2007 and FY 2008.

In addition to equalization, the remaining increase in Real Estate value is due to new construction or normal growth. New construction is expected to increase at a lower rate during FY 2007 and FY 2008 a result of a lack of buildable land in the County. Office construction will continue to primarily be build-to-suit. The two hotels to be completed in 2005 impact the FY 2007 growth estimate. Residential construction is anticipated to be moderate during the forecast period. Overall, increases due to new construction are projected to be 2.10 percent in FY 2007 and 1.80 percent in FY 2008 compared to an increase of 2.69 percent in FY 2006.

FY 2006 Current Personal Property Tax revenue, which represents 16.1 percent of total FY 2006 General Fund revenue, is anticipated to experience growth of 4.9 percent after falling a projected 1.7 percent in FY 2005. Growth in both the vehicle and business components is expected to moderate during the forecast with growth in total Personal Property Tax revenue of 4.0 percent and 3.5 percent in FY 2007 and FY 2008.

Based on the Personal Property Tax Relief Act (PPTRA) of 1998, the Virginia General Assembly approved a plan to eliminate the Personal Property Tax on vehicles owned by individuals. Under the originally approved plan, taxes paid by individuals were to be reduced on the first \$20,000 of value over a five-year period ending in FY 2003. However, due to the State's lower than anticipated General Fund revenue growth and the unanticipated growth in required PPTRA funding, the reimbursement rate has remained at 70 percent since FY 2002. The 2004 General Assembly approved legislation that will continue a 70 percent reimbursement rate through FY 2006, but will cap Personal Property Tax reimbursement in FY 2007 at approximately the FY 2005 level. In subsequent years, the State reimbursement is not expected to cover 70 percent of the Personal Property Taxes paid by residents. Through FY 2007, revenue from the personal property tax paid locally plus state reimbursement should be revenue neutral. The impact on FY 2008, however, is uncertain. At this time, the FY 2008 estimate for Personal Property Tax assumes no revenue impact from the cap on State reimbursements.

Business activity and consumer spending are expected to be moderate during the forecast period. Business, Professional and Occupational Licenses (BPOL) revenue is projected to rise 4.0 percent in each fiscal year while Sales Tax receipts are expected to increase 5.0 percent in FY 2007 and FY 2008.

Interest earned on investments is expected to rise in FY 2007 and FY 2008 based on a forecast of gradual increases in interest rates and growth in the investment portfolio. Since June 2004 when the federal funds rate was 1.0 percent, the Federal Reserve has raised interest rates eight times, to 3.0 percent. The Federal Reserve indicated that gradual increases in interest rates will continue at what they call a measured pace. These adjustments will directly impact the yield earned on the County's investment portfolio. The average annual yield on investments was just 1.04 percent in FY 2004; however, based on current interest rates, the yield on the County investments is expected to rise to 2.23 percent in FY 2005 and to 3.0 percent in FY 2006. During the forecast period, the yield on investments is expected to continue to increase with projections of 3.5 percent in FY 2007 and 4.0 percent in FY 2008.

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Excluding revenues from the Commonwealth of Virginia associated with the reimbursement of Personal Property Taxes, Revenue from the Commonwealth and Federal Government is expected to rise a slight 0.6 percent in FY 2006. Revenue from the Commonwealth and Federal Governments is expected to remain at the FY 2006 level in FY 2007 and FY 2008. Since the majority of the revenue from the state and federal governments are reimbursements associated with expenditure requirements, any increase in revenue is expected to be more than offset with expenditure increases.

The Permits, Fees and Regulatory Licenses category is anticipated to increase \$5.0 million in FY 2006, primarily due to proposed fee increases in Zoning Fees and Land Development Services (LDS) Fees including issuing building permits and inspections. During FY 2007, the second phase of LDS fee adjustments will be implemented, resulting in an increase of \$1.4 million. In FY 2008, LDS fees are projected to remain at their FY 2007 level. It should be noted that the expectation that LDS's Building and Permit fee revenue will not increase assumes a continuation of the same level of building activity projected to be achieved in FY 2007 and should not be viewed as a reduction. Other Permit and Fees and Regulatory Licenses categories are expected to experience modest growth during the forecast period.

In total, General Fund revenues are projected to increase 7.61 percent in FY 2007 and 6.91 percent in FY 2008. Revenue growth rates for individual categories are shown in the following table:

REVENUE GROWTH RATES

Category	FY 2005	FY 2006	FY 2007	FY 2008
Real Estate Tax - Assessment Base	12.04%	23.49%	10.30%	9.20%
Equalization	9.54%	20.80%	8.20%	7.40%
Residential	11.29%	23.09%	9.00%	8.00%
Nonresidential	3.74%	12.74%	5.00%	5.00%
Normal Growth	2.50%	2.69%	2.10%	1.80%
Personal Property Tax - Current ¹	-1.65%	4.86%	4.00%	3.50%
Local Sales Tax	7.58%	5.00%	5.00%	5.00%
Business, Professional and Occupational, License (BPOL) Taxes	6.00%	5.00%	4.00%	4.00%
Recordation/Deed of Conveyance	35.78%	-16.80%	0.00%	0.00%
Interest Rate Earned on Investments	2.23%	3.00%	3.50%	4.00%
Vehicle Decals	1.80%	2.00%	2.00%	2.00%
Building Plan and Permit Fees	-6.19%	20.00%	5.56%	0.00%
Charges for Services	5.17%	10.57%	5.42%	2.33%
State/Federal Revenue ¹	-11.63%	0.57%	0.00%	0.00%
TOTAL REVENUE	6.28%	6.76%	7.61%	6.91%

¹ The portion of the Personal Property Tax reimbursed by the Commonwealth as a result of the Personal Property Tax Relief Act of 1998 is included in the Personal Property Tax category for the purpose of discussion in this section.

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Disbursement Assumptions

Direct Expenditures

As previously mentioned, for the purposes of this forecast, increases in County expenditures have been projected to increase at the rate of estimated growth in County revenues. As such, direct expenditures are shown to increase 7.61 percent in FY 2007 and 6.91 percent in FY 2008. The basic costs of operating County government will have to be accommodated within the projected overall increase for FY 2006 and FY 2007, such as funding pay for performance for employees, market rate adjustments for contractors and inflationary growth, rising health care costs and required contributions for retirement. In addition, we will have to provide for new facilities and service expansions. The Board of Supervisors, at its strategic planning retreat in February 2004 identified priorities for the next four years, including: Public safety and gang prevention; Affordable housing; Environmental protection; Strong investment in education; Transportation improvements; and Revenue diversification to reduce the burden on homeowners. Having these clearly defined priorities will enable the County to focus budget strategies on those initiatives that will result in the greatest return on investment, while balancing the cost to taxpayers.

Transfers Out

School Transfer

The Financial Forecast includes an increase in the School transfer consistent with the rate of revenue growth, 7.61 percent in FY 2007 and 6.91 percent in FY 2008.

Transportation

The transfer requirements of \$24.5 million and \$28.2 million in FY 2007 and FY 2008, respectively, for Metro Operations and Construction reflect annual increases of 15.0 percent based on projected inflationary increases and regional infrastructure requirements for Metrorail and Metrobus service. More moderate increases based on revenue growth are included for County Transit based on projected cost increases in the CONNECTOR bus system and Commuter Rail contributions and the purchase of 15 replacement buses each year.

Debt Service

The Debt Service requirements reflect increases required to support the level of bond sales proposed in the FY 2005 – 2010 Capital Improvement Program (With Future Fiscal Years to 2015).

Paydown

Paydown capital construction includes transfers from the General Fund to support construction and renovation of capital facilities. In FY 2007 and FY 2008, the projected annual transfer for Paydown construction is \$10.0 million per year.

Transfer to Fairfax-Falls Church Community Services Board

The General Fund transfer supporting the Fairfax-Falls Church Community Services Board is consistent with the rate of revenue growth.

Information Technology

A transfer of \$10.0 million has been included in each of the forecast years for information technology (IT). The County's Information Technology Advisory Group (ITAG), a private sector advisory group established by the County Executive to investigate the condition of the County's IT resources, has recommended that annual spending of \$15 million to \$20 million is required to meet IT requirements.

Housing Flexibility

Following the recommendation of the Affordable Housing Preservation Action Committee, the forecast provides the dedication of the projected value of one penny of the real estate tax rate to the Housing Flexibility Fund in order to maintain affordable housing stock in the County.

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Stormwater Management Program

The Forecast for FY 2007 and FY 2008 includes the dedication of the projected value of one penny of the real estate tax rate to fund the environmental and public safety requirements associated with our County stormwater system. Funding is included for essential maintenance and repair in order to protect and extend the County's stormwater infrastructure.

Other Transfers

Other Transfers have been increased by the rate of revenue growth in FY 2007 and FY 2008, or 7.61 percent and 6.91 percent, respectively.